87-461

Supreme Court, U.S.
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No. .....

In the Supreme Court of the United States

OCTOBER TERM, 1987

J & J LOG & LUMBER COMPANY,

Petitioner,

v.

GLOBE MACHINE MANUFACTURING COMPANY,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

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98 pp

QUESTION PRESENTED FOR REVIEW

By way of special jury verdict, J&J Log and Lumber Company ("J&J") was awarded direct and consequential damages against Globe Machine Manufacturing Company ("Globe"). The jury found that Globe was liable under an alter ego theory for breach of a written contract by a controlled third party, as well as for breach of a separate, independent oral contract with J&J.

Globe appealed the award of consequential damages to the United States Court of Appeals for the Ninth Circuit, which has proceeded to issue three different and totally inconsistent decisions in this proceeding. The Ninth Circuit initially affirmed on the basis of Globe's breach of its oral contract with J&J. In a highly unusual and

contradictory series of post-opinion proceedings, the Ninth Circuit granted a petition for rehearing filed by Globe, and issued a second opinion reversing and remanding for further proceedings on a factual issue deemed relevant to the award of consequential damages. J&J thereafter filed its petition for rehearing, which resulted in renewed oral argument and the Ninth Circuit's third and ultimate opinion, which simply reversed the jury verdict without providing for further proceedings on remand.

The question presented by the Ninth Circuit's decision is:

In light of the highly unorthodox appellate treatment of this matter, coupled with the inconsistencies inherent in the progression of decisions rendered, has the Ninth Circuit so far

departed from the accepted and usual course of judicial proceedings as to call for an exercise of this Court's power of supervision to vacate the latest decision or reverse with instructions to remand for further proceedings?

TABLE OF CONTENTS

Page

Opinions Below.....2

Jurisdiction.....2

Statement of the Case.....3

Statement of Facts.....3

Proceedings in the District Court.....4

Proceedings in the Court of Appeals.....7

Reasons for Granting the Writ.....10

This Court Should Exercise Its Power of Supervision as the Ninth Circuit has Dramatically Departed From the Accepted and Usual Course of Judicial Proceedings.....10

Conclusion.....28

Appendix.....App-1

TABLE OF AUTHORITIES

Page

Cases

Armstrong v. Manzo,
380 U.S. 545 (1965).....24

Fuentes v. Shevin,
407 U.S. 67 (1972).....24

Seymour v. Coughlin Co..,
609 F.2d 346 (9th Cir.
1979), *cert. denied*,
446 U.S. 957 (1980).....27

Standard Oil Co. v.
Missouri,
224 U.S. 270 (1912).....25

United States v. First
National Bank,
652 F.2d 882
(9th Cir. 1981).....27

Waggoner v. Dallaire,
649 F.2d 1362
(9th Cir. 1981).....27

Statutory Provisions

28 U.S.C. § 1254(1).....2
Fed. R. Civ. P. 8(c).....6
Fed. R. Civ. P. 16(e).....25, 26

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PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

Petitioner respectfully prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Ninth Circuit entered in this matter on June 19, 1987.

OPINIONS BELOW

The unpublished opinions of the United States Court of Appeals for the Ninth Circuit are set forth in the Appendix, pp. 23-26; 32-46; 48-63. The opinion of the United States District Court for the District of Oregon, entered on March 26, 1984, is set forth in the Appendix, pp. 2-18.

JURISDICTION

The judgment and opinion of the United States Court of Appeals for the Ninth Circuit was entered on June 19, 1987. A timely petition for rehearing was denied on August 10, 1987. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATEMENT OF THE CASE

Statement of Facts

In 1980, Hildebrand North America, Inc. ("HNA") entered into contracts to design and manufacture dry kilns for J&J. In July, 1981, and while work on the project was in progress, Globe acquired majority stock ownership and control over the parent of HNA, and thereafter installed one of its employees as HNA's new president. The evidence received at trial established that thereafter Globe exercised actual control over the operations of HNA. HNA subsequently abandoned performance of the contract, and engaged in certain conduct designed to frustrate J&J's efforts to complete the job itself.

At the time of Globe's takeover of HNA in July, 1981, Globe and J&J entered

into an oral contract, whereby Globe, for separate and independent consideration, agreed to complete the kiln project for J&J. Globe breached its promise.

As a result of the breaches of contract by Globe and HNA, J&J sustained actual and consequential damages.

Proceedings In The District Court

J&J commenced suit against Globe in the United States District Court for the District of Oregon, seeking damages on two parallel theories: (1) breach of the direct oral agreement between Globe and J&J to complete the project; and (2) Globe's liability under an alter ego theory for the abandonment by HNA of its written contracts with J&J. On the last court day before trial, Globe filed a memorandum which argued, for the first

time, that certain warranty language contained in the written contract between HNA and J&J limited any recovery of consequential damages against Globe. This issue had not been asserted by Globe as an affirmative defense, nor had it been raised in the pretrial order lodged by the parties with the trial court several months earlier.

Globe objected to J&J's evidence of lost profits during trial on the basis of the warranty clause in the written contract. The district court allowed the evidence to be received, reserving a determination of the issue until post-trial submissions had been received. No jury instructions were requested by either party relating to the application of the written warranty provision.

During trial, J&J further introduced evidence to show that Globe

had engaged in "improper conduct" in its actual control over HNA, to the detriment of J&J. Such proof was necessary to establish Globe's alter ego liability for HNA's breach of contract with J&J.

The jury sustained both legal theories by way of special verdict in favor of J&J, awarding direct and consequential damages in the full amount of the prayer. Globe moved for judgment notwithstanding the verdict, again contending that the award of consequential damages was limited by the provisions of the written HNA contract.

In its Memorandum and Order dated March 16, 1984 (App. pp. 2-18), the district court ruled that Globe had waived its objection by failing to present it as an affirmative defense as required by Fed. R. Civ. P. 8(c). The district court further found that, in

any event, the evidence and jury finding of "improper conduct" on the part of Globe was tantamount to bad faith, thus precluding Globe from relying upon the exculpatory language. There was no ruling on the legal issue whether the warranty limitation of damages provision would be applicable following a total abandonment of the contracts, which was heavily contested between the parties. Judgment was subsequently entered on the jury's verdict in favor of J&J.

Proceedings In The Court Of Appeals

The Ninth Circuit has issued three different and totally inconsistent decisions in this proceeding. On May 15, 1986, the Court of Appeals initially affirmed the jury verdict in an unpublished memorandum decision. (App. pp. 23-26). Because the oral contract

between Globe and J&J was completely separate and independent of the written contract of HNA, and because Globe presented no evidence that the parties intended the warranty provisions of the written contract to be incorporated in the oral contract, the Ninth Circuit held that Globe could not rely on the written exculpatory language so as to avoid its direct oral contractual liability.

Globe thereafter filed a petition for rehearing, which resulted in the withdrawal of the first decision and the entry of a second memorandum decision dated December 2, 1986. (App. pp. 30-46). In its second opinion, the Court of Appeals found that the oral contract "necessarily incorporated" the written warranty provision of the HNA contract. The Ninth Circuit also ruled

that there was no waiver resulting from the failure of Globe to assert the limitation of damages provision as an affirmative defense. However, the Ninth Circuit disagreed with the finding of the district court that the "improper conduct" of Globe was tantamount to "bad faith" thus precluding it from relying upon the exculpatory language, and thus the Court of Appeals *remanded* for further proceedings.

J&J thereafter filed its petition for rehearing, noting cumulative factual and procedural errors in the second opinion. Following renewed oral argument, the Ninth Circuit on June 19, 1987, withdrew its second opinion, and entered its third and ultimate memorandum decision. (App. pp. 47-63). In its final ruling, the Court of Appeals reiterated many of its findings

contained in its second opinion, but held further that "J&J never presented a case on the bad faith issue," and proceeded to reverse the jury verdict, eliminating the provision for further proceedings on remand. J&J thereafter filed a petition for rehearing directed solely to the failure to remand for further proceedings on the "bad faith" issue. On August 10, 1987, the Ninth Circuit denied J&J's petition.

REASONS FOR GRANTING THE WRIT

THIS COURT SHOULD EXERCISE ITS POWER OF SUPERVISION AS THE NINTH CIRCUIT HAS DRAMATICALLY DEPARTED FROM THE ACCEPTED AND USUAL COURSE OF JUDICIAL PROCEEDINGS.

J&J recognizes that the supervisory power of this Court to correct departures of federal courts of appeals from accepted and usual judicial proceedings must be sparingly granted. Such an

unusual situation is presented in this Petition.

The procedural history is characterized by developments that can only be described as bizarre, and is further underscored by a disturbing progression of everchanging and inconsistent appellate decisions which cannot be supported by the record as submitted. Most disturbingly, the handling of this matter by the Ninth Circuit clearly reflects a serious misunderstanding, if not total confusion, of the factual, legal and procedural background for the case. As such, it is respectfully submitted that the actions of the Ninth Circuit in this proceeding require this Court to exercise its supervisory powers in either vacating the latest decision or in fashioning some other appropriate remedy which will not only preserve the

rights of the litigants, but also restore the proper role of the federal courts of appeals in resolving appellate matters.

Post-submission orders by the Ninth Circuit were unorthodox and clearly revealed serious confusion about the case.

Virtually from the outset, the proceedings in the Ninth Circuit have been marked by an unprecedented series of events which, coupled with inconsistent decisional treatment, have rendered the case a marked departure from the accepted and usual course of judicial proceedings.

Shortly after oral arguments the Court of Appeals issued a highly unusual order inquiring as to the settlement posture of the case, offering to vacate the order of submission if the parties wished to use "the settlement mechanisms" of the Ninth Circuit. (App.

p. 19-20). Following consideration of correspondence received from counsel, the Court of Appeals declined to vacate its previous order submitting the case. (App. pp. 21-22).

Nearly 14 months after oral argument, the first decision of the Ninth Circuit was entered. (App. pp. 23-26). As noted previously, the jury verdict was affirmed in favor of J&J, based upon a ruling that Globe had failed to prove that the terms of the written HNA contract had been incorporated into the separate and independent oral contract.

Globe thereafter filed its petition for rehearing. In response, the Ninth Circuit entered an Order dated June 20, 1986, requesting the parties to brief the issue of whether the jury verdict could justify affirmance on a theory of

tortious interference with contract by Globe. (App. pp. 27-29).

Both Globe and J&J agreed in their submissions to the Ninth Circuit that tortious interference with contract was never a theory relied upon by J&J at trial. Indeed, the elements of that tort were totally inconsistent with the evidence presented by J&J in order to establish alter ego liability on the part of Globe.

The June 20, 1986 order from the Ninth Circuit clearly evidenced an unprecedented degree of misapprehension and confusion by the Court of Appeals as to the nature of the proceedings below and as to the factual and legal issues for resolution on appeal.

Following the second decision J&J requested a reconstituted panel, as the confusion and misunderstanding by the Ninth Circuit was clearly irremediable.

On December 1, 1986, the second decision was entered by the Ninth Circuit, reversing and remanding to the trial court for further proceedings as to whether the conduct of Globe was tantamount to "bad faith", a finding that would preclude a reliance upon any written exculpatory language. In order to accomplish this remarkable turnabout, the Ninth Circuit predicated "error" on trial court rulings that had never been made, reversed a discretionary trial court ruling without finding an abuse of discretion, resolved several factual issues as a matter of law, and decided the case on a basis that Globe had failed to urge on appeal.

Based upon the history of the appellate proceedings as of that date, J&J filed its petition for rehearing, suggesting that renewed oral argument

before a *reconstituted panel* would be appropriate. Again, it was clear that the Ninth Circuit, over the passage of time or otherwise, had put out of focus the central issues of the case, and was laboring under severe misapprehensions about the factual and procedural background of the litigation. It was equally clear that the level of confusion and misunderstanding had reached the stage where it was irremediable.

The third and latest decision of the Ninth Circuit, eliminating any further proceedings on remand, confirms that the appellate handling of the case at that stage was out of control.

Following renewed oral argument *before the same panel*, the Ninth Circuit has, in its third and ultimate decision, clearly justified J&J's misgivings as set forth in its initial petition for rehearing. As a result of the third and

final decision, the Ninth Circuit has, remarkably, precluded any remand proceedings on factual issues that the Court of Appeals previously found to be pivotal for total resolution of the case.

In its second opinion, the Court of Appeals found that even though J&J had presented evidence to the jury on Globe's improper conduct -- a requisite under Oregon law for establishing alter ego liability -- the trial court erred in holding that "improper conduct" was the equivalent of "bad faith" for purposes of precluding Globe's reliance on the limitation of liability provision:

> "While it is true that bad faith may prevent a defendant from asserting contractual provisions limiting damages, the determination of the existence of bad faith is a question of fact independent of the determination of 'improper

> conduct' in connection with plaintiff's alter ego theory." (App. p. 45).

The case was remanded for further proceedings.

Although J&J may have disagreed with the analysis of the Ninth Circuit in its second opinion as to the "bad faith" issue, it was confident that on remand "bad faith" could be established before an appropriate trier of fact, thus resolving the issue. J&J had more than adequately presented at trial evidence of Globe's "improper conduct" for purposes of the alter ego theory. This same evidence obviously would have served as the basis for a further finding on remand of "bad faith".

In its third opinion, the Ninth Circuit has, in a totally unjustifiable and erroneous ruling, precluded J&J from presenting evidence of "bad faith" to a

trier of fact in the future. The Ninth Circuit's treatment in this regard further underscores the apparent confusion and misapprehensions under which it has labored throughout this appellate proceeding. Again, in its second opinion, the Ninth Circuit took issue with the trial court for ruling that the evidence of improper conduct introduced and received during trial by J&J was sufficient to establish conclusively a corollary finding of "bad faith". The Ninth Circuit held that as a different standard might be applicable, the separate question of fact had to be pursued further on remand. In its third opinion, however, the Court of Appeals remarkably states that J&J has failed to present any evidence on bad faith when, by its own previous analysis, the ultimate question

was not one of the evidence presented, but rather what standard was employed in analyzing the evidence.

Further, the Ninth Circuit in its third and final opinion noted J&J's failure to request a jury instruction on the issue of bad faith as being an indication that it presented no evidence during trial on that issue. Again, this emphasizes the Court of Appeal's total misunderstanding of the procedural background of this litigation. The trial court specifically reserved resolution of the applicability of the exculpatory language until post-trial briefing. That being so, neither J&J *nor Globe* requested jury instructions on the bad faith issue.

The elimination of further proceedings on remand further precludes resolution of a foundational legal issue.

The ultimate indication that the

Ninth Circuit has departed from the accepted and usual course of judicial proceedings is its complete disregard of the pivotal legal issue at the core of the dispute between the parties: the applicability, after an abandonment of contract, of a limitation of damages clause contained in a warranty provision.

This issue has been briefed extensively by both Globe and J&J at every stage of the proceedings, but has never been resolved at the either the trial court level or by the Ninth Circuit. It is understandable that the Court of Appeals would attempt to shape its analysis to fit the opinion of the district court, and it has done so, ruling on both the issues of Globe's waiver of the defense and bad faith. However, by simply reversing the

verdict, the most recent decision of the Ninth Circuit has the potential impact of precluding the ultimate resolution of this critical element of the case. Again, the Court of Appeals has simply lost sight of what this case is all about.

The final Ninth Circuit treatment of the "bad faith" issue was rendered *sua sponte*, and J&J has never been afforded the opportunity to respond.

In its second decision the Ninth Circuit remanded for further proceedings to analyze the evidence utilizing a "bad faith" standard, as opposed to an "improper conduct" standard as employed by the trial court. However, instead of simply denying J&J's petition for rehearing, which was filed thereafter, the Ninth Circuit went the final step in its march of inconsistency and dismissed the claim for lost profits by ruling, as

a matter of law, that J&J had "failed to present a case on the bad faith issue" at the time of trial. This ruling has no procedural foundation.

Throughout its briefing on this issue, which spanned over three years, Globe at no time argued that J&J had failed to present a case on bad faith. To the contrary, the argument of Globe in this regard is that the issue should have been a matter for the jury, and that the trial court erred in deciding this issue itself.

Prior to the Ninth Circuit's third and final decision, there had simply been no issue raised questioning whether J&J had presented evidence at trial which might support a finding of bad faith by a trier of fact. Again, the only question was whether the trial court used the proper standard. As

such, J&J obviously has had no notice of what, as it turns out, has become the determinative feature of this case; nor has J&J been afforded the opportunity to respond to this issue.

Fundamental notions of proper adjudicatory power, together with obvious due process undercurrents, dictate that a court must refrain from exercising its powers until and unless the party impacted has received adequate notice and an opportunity to be heard. *Fuentes v. Shevin*, 407 U.S. 67, 80 (1972). These rights "must be granted at a meaningful time and in a meaningful manner." *Armstrong v. Manzo*, 380 U.S. 545, 552 (1965). Further, a court cannot enter a judgment which is beyond the scope of the issues presented, or which is not responsive to the cause of action on which the proceeding was

based. *Standard Oil Co. v. Missouri*, 224 U.S. 270, 281 (1912).

The Ninth Circuit has totally ignored the pretrial order provisions of Rule 16 of the Federal Rules of Civil Procedure in finding that Globe had not waived application of the written limitation of damages clause.

The Court of Appeals has held that the terms of a contract that has been introduced into evidence and upon which an action is based need not be raised as an affirmative defense. While J&J certainly takes issue with this ruling, even more disturbing is the Ninth Circuit's total failure to respect the district court's broad discretionary powers to preclude an issue from being introduced at the time of trial when it has not been set forth in the pretrial order.

The final pretrial order was lodged with the trial court nearly six months

before trial. In it, J&J expressly alleged that it was entitled to recover consequential damages. The opposing factual and legal contentions set forth by Globe failed to make any assertions whatsoever that consequential damages could be excluded or limited due to contractual provisions. Even assuming that the Ninth Circuit was correct in ruling that such a defense need not be affirmatively pleaded, there is no question but that such a significant issue was required to be raised in the pretrial order contentions.

Rule 16(e) of the Federal Rules of Civil Procedure provides that the statement of issues in the pretrial order has a preclusive effect, and that after such order has been lodged it may be modified only to prevent manifest injustice. The obvious policy reason

behind this is to prevent litigants from employing tactics of ambush and surprise; and indeed the Ninth Circuit has repeatedly held that issues not incorporated in the pretrial order are waived unless the trial court, in the exercise of its discretion, permits an amendment of the order. *United States v. First National Bank*, 652 F.2d 882, 886 (9th Cir. 1981); *Waggoner v. Dallaire*, 649 F.2d 1362 (9th Cir. 1981); *Seymour v. Coughlin Co.*, 609 F.2d 346 (9th Cir. 1979), *cert. denied*, 446 U.S. 957 (1980).

Here, Globe never attempted to show manifest injustice; indeed, Globe never moved for leave to amend the pretrial order for purposes of preserving its defense to J&J's claim for lost profits. The Ninth Circuit made no finding of an abuse of discretion or

manifest injustice in overruling the trial court's holding of a waiver of the defense by Globe. Having failed to find such an abuse of discretion, the Ninth Circuit had no procedural basis for reversing the award of consequential damages.

CONCLUSION

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Respectfully submitted,

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September 15, 1987

APPENDIX

Page

Memorandum and Order of District Court (March 25, 1984).....App.-2

Order of Ninth Circuit Relating to Settlement (March 12, 1985).....App.-19

Order of Ninth Circuit Declining to Vacate Order of Submission (April 23, 1985).....App.-21

Memorandum Decision of Ninth Circuit ("First Opinion") (May 15, 1986).....App.-23

Order of Ninth Circuit Relating to Further Briefing (June 20, 1986).....App.-27

Order of Ninth Circuit Withdrawing Memorandum Decision of May 15, 1986 (December 2, 1986).....App.-30

Memorandum Decision of Ninth Circuit ("Second Opinion") (December 2, 1986).....App.-32

Order of Ninth Circuit Withdrawing Memorandum Decision of December 2, 1986 (June 19, 1987).....App.-47

Memorandum Decision of Ninth Circuit ("Third Opinion") (June 19, 1987).....App.-48

IN THE UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF OREGON

J & J LOG & LUMBER COMPANY, a New York corporation,	)	
Plaintiff,	)	CIVIL NO. 81-874-BE
v.	)	
GLOBE MACHINE MANUFACTURING COMPANY, a Washington corporation,	)	MEMORANDUM and ORDER
Defendant.	)	

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Plaintiff J & J Log and Lumber Company (J&J) brought this action against defendant Globe Machine Manufacturing Company (Globe) for breach of a contract to construct six dry kilns. The jury awarded plaintiff the full amount of requested damages. Defendant makes this post-trial motion to include consequential damages from plaintiff's award. I find defendant's motion to be without merit and therefore deny it.

Facts

On November 18, 1980, J&J entered into a written contract with Hildebrand

North America (HNA) for the manufacture and installation of six dry kilns. HNA was a wholly-owned subsidiary of Wood Technology Systems, Inc. Wood Technology Systems was, in turn, a holding company in which Globe acquired a controlling interest during the course of the parties' relationship.

On August, 1981, HNA discontinued work on the partially completed dry kilns. Plaintiff presented evidence to show that HNA removed not only its work force from the job site but also the construction plans and some kiln equipment which made plaintiff's completion of the project more costly.

Plaintiff brought this action in September, 1981, alleging that defendant was responsible for the breach of two agreements. First, plaintiff alleged that Globe breached an oral agreement in which, among other things, Globe

guaranteed completion of the J&J/HNA written contract. Second, plaintiff alleged that Globe exercised its control over HNA improperly, causing HNA to breach the J&J/HNA written contract.

For the sake of clarity, the kiln construction contract between J&J and HNA shall be referred to as the J&J/HNA written contract and the oral agreement between J&J and Globe shall be referred to as the J&J/Globe oral agreement.

Trial was ultimately set for September, 1983. In pretrial conference, one week prior to trial, defendant raised the issue that any recovery by plaintiff of consequential damages was barred by exculpatory language contained within the warranty section of the J&J/HNA kiln contract. Plaintiff denied this contention. Both parties prepared memorandums for the court on this issue prior to trial.

I ruled that I would consider this matter further but that plaintiff would be allowed to present evidence of consequential damages during trial. My decision was based in part upon defendant's violation of Fed. R. Civ. P. 8(c) which requires that an affirmative defense of this nature be set forth in a responsive pleading.

At the conclusion of trial, the jury found for plaintiff on both of the alternative grounds alleged. The special verdict read as follows:

> CONTRACT THEORY
>
> 1. Did plaintiff and defendant enter into a contract on July 21, 1981, in which J&J agreed to:
>
> a. Release its option to purchase five percent of Hildebrand North America stock,
>
> b. Persuade Steve Simon to transfer his stock in wood Technology to Globe, and
>
> c. Pay the balance due under its contracts with Hildebrand, and in which Globe agreed to:
>
> a. See that the J & J contract would be completed,

b. Post a $400,000 bond on the project, and,

c. Allow J & J to withdraw its $500,000 letter of credit:

Yes __X__ No ____

ALTER EGO THEORY

2. At the time Hildebrand ceased work on plaintiff's project (a) did Globe actually control Hildebrand, and (b) engage in improper conduct in that control, and (c) thus cause harm to plaintiff by the improper conduct? Check "Yes" below if your answers to a, b, and c are all "Yes". Check "No" if your answer to a, b, or c is "No".

Yes __x__ No ____

If you answered "No" to both questions (1) and (2), your verdict is for defendant. The foreman should sign and date this verdict form, then signal the bailiff that you have completed your deliberations. If you answered "Yes" to either questions (1) or (2), or both, proceed to the next question.

3. What are the damages?

a. Cost of completing the project over and above the contract price (if any) $262,665.11

b. Lost profits (if any) $1,368,749.00

Defendant now moves for a motion notwithstanding the verdict to overturn the jury award of consequential damages.

DISCUSSION

Defendant's Failure to Plead an Affirmative Defense

Federal Rule of Civil Procedure 8(c) requires that an affirmative defense be set forth in a responsive pleading. A limitation of liability defense, such as the one raised in this case, is an affirmative defense that must be responsively pleaded. 5 Wright & Miller, Federal Practice & Procedure, Civil §1272 (1969). Because the defense was not affirmatively pleaded, it was waived. See Jacobsen v. Massachusetts Port Authority, 520 F.2d 810 (1st Cir. 1975) (Court barred defendant from raising statutory limitation of liability defense at trial); Automated Medical Labs v. Armour Pharmaceutical, 629 F.2d 1118 (5th Cir. 1980) (Court barred statute of frauds defense raised in trial memo); Funding Systems Leasing

Corp. v. Pugh, 530 F.2d 91 (5th Cir. 1976) (Court barred statute of frauds defense raised in motion for summary judgment but not raised in pleadings or pretrial order); Berkeley Unified School District v. James I. Barnes Constr. Co., 112 F. Supp 396 (N.D. Cal. 1953) (Court held improper a motion to dismiss based on a liquidated damages provision. Court required that defendant affirmatively plead this defense).

In Automated Labs, 629 F.2d at 1122, Judge Politz articulates the reasoning behind this rule. He states:

> Although absolute specificity in pleading is not required, fair notice of the affirmative defense is. Fed. R. Civ. P. 8(f). Under the liberalized pleading guidelines codified in the Federal Rules, ample opportunity to amend pleadings exists with leave to be freely given. Fed. R. Civ. P. 15(a). Thus, while one wishing to assert an affirmative defense has every opportunity to do so, it must be done at a time and in a

> manner which is consistent with the language and spirit of the Federal Rules. The court and the opposing party must be timely advised of the intended defense.

In the instant case defendant had several years in which to amend its pleadings. Contrary to Rule 8(c), defendant waited until the eve of trial to make its defense known.

Defendant now contends that the untimeliness of the defense did not prejudice the plaintiff. I find to the contrary. Besides completing its final trial preparation within the few days prior to trial, plaintiff now had to prepare a memorandum for the court on this issue and develop new trial strategies. These are precisely the types of things that Fed. R. Civ. P. 8(c) seeks to prevent for they put the plaintiff at a severe disadvantage.

Besides defendant's failure to comply with the Federal Rules, the outcome of the trial provides additional reasons for upholding the jury verdict.

The Verdict's Alternative Grounds

The basis for defendant's affirmative defense is that the exculpatory language within the J&J/HNA contract precludes any recovery by plaintiff of consequential damages. For defendant's argument to be successful, defendant must establish that the exculpatory language within the J&J/HNA contract operates to bar the recovery of consequential damages from both of the alternative grounds supporting the judgment. These alternative grounds include a) that defendant controlled HNA and engaged in improper conduct causing HNA to breach the J&J/HNA contract and b) that defendant breached the J&J/Globe oral agreement in which, among other

things, Globe guaranteed completion of the dry kilns.

Before deciding this issue, I note that the J&J/HNA contract provides that it shall be construed in accordance with New York law. Neither party argues with the contention that New York law controls the case.

Ground 1 - Globe's Improper Conduct Causing HNA's Breach

Defendant contends that the exculpatory language within the J&J/HNA contract precludes plaintiff from any recovery of consequential damages awarded plaintiff for Globe's improper control of HNA. This is contrary to New York case Law. In County Asphalt, Inc. v. Lewis Welding and Engineering Corp., 323 F. Supp. 1300 (S.D.N.Y. 1970), the court stated that it would bar defendant from asserting exculpatory language where the defendant breached in bad

faith its contract to construct certain concrete manufacturing plants. I find this case analogous with the instant case where defendant acquired control of HNA and then engaged in "improper conduct" in that control causing HNA to breach its contract with J&J. Accordingly, defendant is estopped from raising this defense to preclude recovery of consequential damages in alternative ground number one.

Ground 2 - Globe's Breach of the Oral Agreement

Defendant's argument is even less persuasive with respect to the jury's finding that Globe breached its oral agreement with J&J. Defendant is attempting to apply the exclupatory language from the J&J/HNA written contract to limit damages resulting from defendant's breach of the J&J/Globe oral agreement. These are two independent

contracts involving different parties and supported by separate consideration. Although the J&J/Globe oral agreement does include defendant's guaranty to complete the J&J/HNA written contract, there has been no showing that the parties intended to limit damages for breach of the oral agreement in accordance with the exculpatory language in the written contract. Without this showing of intent, the court will not apply the limitations from the J&J/HNA contract to the J&J/Globe contract. See Frierson v. International Agricultural Corp., 148 S.W. 2d 27, 34-36 (Tenn App. 1940); McPherson v. Longview United Pentacostal Church, 540 S.W. 2d 424, 431 (Tex. Civ. App. 1976); M. J. Delaney v. Murchison, 393 S.W. 2d 705 (Tex. Civ. App. 1965).

About as much as can be said for defendant's argument is that it raises a

factual question as to whether the parties intended to adopt the limitation of liability provision contained in the written contract. Defendant could have but did not raise this issue during trial. The question of fact, therefore, must be deemed to have been found in favor of the judgment. See M. J. Delaney, 393 S.W. 2d at 705.

Defendant contends that it did show the parties' intention to adopt the exculpatory language. Defendant refers to the testimony of J&J's president, James Williams, that all of the J&J/HNA contract was included within the J&J/Globe oral agreement. It is logical to assume from Mr. Williams' statement that the parties intended the contract specifications within the J&J/HNA contract be followed in the event it became necessary for Globe to complete the kilns. It is not logical to assume

that the parties intended to adopt the ambiguous exculpatory language contained within the warranty section of the kiln contract. Mr. Williams' statement, by itself, is insufficient to warrant such a finding of intent. Thus, defendant's argument to preclude the recovery of consequential damages from the second alternative ground is without merit.

Defendant's motion to overturn the jury's award of consequential damages is therefore denied.

In addition to defendant's argument concerning consequential damages, defendant raises numerous other grounds in support of his motion for judgment notwithstanding the verdict, or in the alternative, for a new trial.

The well-recognized standard of review is that a trial court may grant a judgment n.o.v. "only when the evidence 'viewed most favorably to the party

against whom the motion is directed cannot support a verdict in that party's favor.'" Criswell v. Western Airlines, Inc., 709 F.2d 544,551 (9th Cir 1983). The trial court should resolve all inferences in favor of the party with the burden of persuasion, without weighing contradictory evidence or passing on witness credibility. California Computer Products, Inc. v. International Business Machines Corporation, 613 F.2d 727, 733 (9th Cir 1979). In the instant case, I find that the evidence supports the jury's verdict. Contrary to defendant's contention, I find no ground on which to support a judgment n.o.v. or new trial. Accordingly, defendant's motion

is denied and plaintiff's motion for Entry of Judgment is granted.

DATED this 16 day of March, 1984.

/s/ Robert C. Belloni
United States District Judge

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

J & J LOG & LUMBER COMPANY, a New York corporation,	)	
Plaintiff-Appellee,	)	No. 84-3788
v.	)	ORDER
GLOBE MACHINE MANUFACTURING COMPANY, a Washington corporation,	)	
Defendant-Appellant.	)	

Before: KENNEDY and NORRIS, Circuit Judges, and STEPHENS,* District Judge.

At oral argument counsel were asked if settlement has been explored. If substantial settlement negotiations commence, or if the parties wish to use the settlement mechanisms of this court, the Clerk should be so advised

* Honorable Albert Lee Stephens, Senior U.S. District Judge for the Central District of California, sitting by designation.

promptly. The panel would then consider whether to vacate the order of submission. The case is ordered submitted at this time.

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

J & J LOG & LUMBER COMPANY, a New York corporation,	)	
Plaintiff-Appellee,	)	No. 84-3788
v.	)	
GLOBE MACHINE MANUFACTURING COMPANY, a Washington corporation,	)	ORDER
Defendant-Appellant.	)	

Before: KENNEDY and NORRIS, Circuit Judges, and STEPHENS,* District Judge.

On consideration of the correspondence received from counsel for the respective parties, the court declines

* Honorable Albert Lee Stephens, Senior United States District Judge for the Central District of California, sitting by designation.

to vacate its previous order that this case be submitted.

/s/
UNITED STATES CIRCUIT JUDGE

NOT FOR PUBLICATION
UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

J & J LOG & LUMBER COMPANY, a New York corporation,	)	No. 84-3788
Plaintiff-Appellee,	)	D.C. No. CV 81-874-BE
v.	)	MEMORANDUM*
GLOBE MACHINE MANUFACTURING COMPANY, a Washington corporation,	)	
Defendant-Appellant.	)	

Appeal from the United States
District Court
for the District of Oregon
The Honorable Robert C. Belloni,
District Judge Presiding
Argued and Submitted March 5, 1985
Portland, Oregon

Before: KENNEDY and NORRIS, Circuit Judges, and STEPHENS,** District Judge

* This disposition is not appropriate for publication and may not be cited to or by the courts of this circuit except as provided by 9th Cir. R. 21.

** Honorable Albert Lee Stephens, Senior United States District Judge for the Central District of California, sitting by designation.

Globe Machine Manufacturing Company appeals from the jury's award of lost profits in favor of J & J Log & Lumbering Company. The district court denied Globe's request for a judgment notwithstanding the verdict or, in the alternative, a new trial. We have jurisdiction under 28 U.S.C. 1332, and affirm.

Globe argues that its oral agreement with J & J incorporated the damages limitation clause from the written contract between J & J and HNA. Globe bore the burden of proving that the parties intended to limit damages for breach of the oral agreement in accordance with the exculpatory language in the written contract. The case was tried under the theory that the oral agreement represented an independent promise by Globe to complete the

project for J & J. To the extent that Globe attempted to pursue a surety theory below, such a theory was inadequately preserved for appeal. Thus, we reject Globe's argument that the oral agreement created a surety relationship and automatically incorporated the damages limitation set forth in the written contract.

The intent of the parties at the time a contract is executed is a question of fact for the jury. May v. Nevada Irrigation Dist., 600 F.2d 1280, 1282 (9th Cir. 1979). We agree with the district judge that Globe offered no evidence to the jury that the parties intended to incorporate the damages limitation clause. Indeed, Globe does not appear to have even argued this fact issue to the jury. Nor did Globe request a jury instruction on the issue. In short, we see no reason to

disturb the decision below. Because we conclude that Globe raised no fact issue concerning the application of the damages limitation clause to its agreement with J & J, we need not reach the question of waiver or of "improper conduct."

AFFIRMED

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

J & J LOG & LUMBER COMPANY, a New York corporation,	)	No. 84-3788
Plaintiff/Appellee,	)	D.C. No. CV-81-874-BE
v.	)	ORDER
GLOBE MACHINE MANUFACTURING COMPANY, a Washington corporation,	)	
Defendant/Appellant.	)	

Appeal from the United States
District Court
for the District of Oregon

Before: KENNEDY and NORRIS, Circuit Judges, and STEPHENS,* District Judge

Appellant, Globe Machine Manufacturing Company, is requested to supplement its petition for rehearing by filing within fourteen days from the

* Honorable Albert Lee Stephens, Senior U.S. District Judge for the Central District of California, sitting by designation.

date of this order a brief, not to exceed ten pages, addressing the following issues:

1. Does the affirmative answer to special verdict number 2 justify affirmance on a tort theory of tortious interference by Globe with the contractual obligations between HNA and J & J?

2. If so, is the issue of consequential damages irrelevant in this case?

3. Was the case fairly tried on that theory, and is the theory supportable in light of the trial judge's jury instructions?

Thereafter, appellee, J & J Log & Lumber Company, within fourteen days, shall file an answer, not to exceed fifteen pages, to Globe's petition for rehearing, responding to the points Globe makes in its initial petition for

rehearing and in its supplemental brief.

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

J & J LOG & LUMBER COMPANY, a New York corporation,	)	No. 84-3788
Plaintiff-Appellee,	)	D.C. No. CV-81-874-BE
v.	)	ORDER
GLOBE MACHINE MANUFACTURING COMPANY, a Washington corporation,	)	
Defendant-Appellant.	)	

Appeal from the United States District Court for the District of Oregon

Before: KENNEDY and NORRIS, Circuit Judges, and STEPHENS,* District Judge

The petition for rehearing is granted. No further oral argument is required. The previous memorandum, filed May 15, 1986, is withdrawn, and a

* Honorable Albert Lee Stephens, Senior U.S. District Judge for the Central District of California, sitting by designation.

new memorandum disposition is filed on this date.

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

J & J LOG & LUMBER COMPANY, a New York corporation,	)	No. 84-3788
Plaintiff-Appellee,	)	D.C. No. CV 81-674-BE
v.	)	MEMORANDUM*
GLOBE MACHINE MANUFACTURING COMPANY, a Washington corporation,	)	
Defendant-Appellant.	)	

Appeal from the United States
District Court
for the District of Oregon
Honorable Robert C. Belloni,
District Judge, Presiding
Argued and Submitted: March 5, 1985
Portland, Oregon

Before: KENNEDY and NORRIS, Circuit Judges, and STEPHENS**, District Judge

* This disposition is not intended for publication and shall not be cited as precedent. Rule 21, Rules of the Ninth Circuit.

** Honorable Albert Lee Stephens, Jr., Senior United States District Judge for the Central District of California, sitting by designation.

On November 18, 1980, J & J Log entered into a written contract with Hildebrand North America, Inc. (HNA) for the design and construction of six lumber kilns and a wood-fired steam generating system in Dover Plains, New York, J & J's place of business. During negotiations between the parties, J & J insisted on a penalty clause of $500.00 per day in the event that HNA failed to complete the contract by October 31, 1981. HNA, in turn, insisted on limiting its liability for late completion to a maximum late penalty of five percent of the contract price. The contract contained a limited warranty for repair and/or replacement of defective parts. The contract also excluded special or consequential damages sustained by J & J "from any cause."

HNA failed to complete the J & J contract in a timely manner. The contract provided for delivery on or before May 18, 1981. By late summer of 1981, only about 55% of the contract had been performed, although J & J had already paid 80% of the payments it owed under the contract.

HNA never operated on a positive cash flow after 1980. Upon discovering in June 1981 that completion of the J & J/HNA contract would be jeopardized unless HNA received financial assistance, the president of J & J agreed to post a $500,000 letter of credit for HNA's use as operating capital. In return, J & J received an option to purchase five percent of the HNA stock and a security interest in everything owned by HNA and Wood Technology, Inc. (Wood Tech), HNA's parent corporation.

Prior to July 20, 1981, Globe Machine Manufacturing Co., (Globe) owned 45% of the outstanding shares of Wood Tech. In late July, Globe acquired a controlling interest in Wood Tech by obtaining a proxy from another Wood Tech shareholder. Globe then called a meeting of the shareholders of Wood Tech. The president of J & J flew from New York to Oregon to attend the shareholders meeting in order to protect J & J's interest in HNA and Wood Tech. At the meeting, Globe elected new directors and officers for HNA. The new president of Wood Tech and the president of J & J had a private conference that same morning. The parties disagree about exactly what transpired in that conference.

The president of J & J, Williams, testified that the two men agreed that Globe would see that the J & J project

was completed, would post a bond on the project and would release J & J from its underlying letter of credit obligations. In return, Williams claimed, J & J agreed to release its option to purchase 5% of HNA, to pay the balance of the contract price still owing HNA in advance and to help Globe obtain additional shares in Wood Tech. In contrast, the president of Wood Tech, Bamford, testified that, although he acknowledged Williams' proposals, he was in no position to agree to anything on behalf of Wood Tech at that point, and accordingly, never formed an agreement with Williams.

Work on the J & J contract subsequently ceased, and J & J filed suit against Wood Tech and HNA for the return of its letter of credit. J & J ultimately undertook completion of the project itself. HNA responded by taking

certain actions such as obliterating J & J's name from crated equipment sitting in HNA's yard that had been destined for shipment to J & J, and locking up the blueprints and drawings for the J & J job.

J & J completed the project in early June, 1982, at a cost of $262,665.11. The HNA/J & J contract had provided for completion of the kilns by May 17, 1981. J & J filed suit in the district court for breach of contract by Globe. J & J claimed at trial that it had suffered a delay of seven months, a time period figured by a starting date for the penalty clause under the written contract of November 1, 1981, and a completion date for the project of the end of May, 1982.

At trial, J & J proceeded on a breach of contract theory alleging breach of the oral agreement made

between the presidents of Wood Tech and J & J at the Wood Tech's shareholders' meeting, and also claiming that Globe was liable as the alter ego of HNA for breach of the underlying written construction contract. In its pretrial memorandum, Globe, for the first time, raised the defense that J & J was not entitled to any consequential damages under the clause in the written contract preventing such damages from accruing against the seller. At trial, the district court allowed J & J to introduce evidence of its lost profits (consequential damages), but refused to allow Globe to present any evidence regarding the damages limitation clause.

The jury returned a special verdict in favor of plaintiff J & J. The verdict included an award for the cost of completion of the contract, and a

separate award for consequential damages in the form of lost profits stemming from the delay in completion of the contract. In a Memorandum and Order denying Globe's Motion for Judgment Notwithstanding the Verdict, the trial judge found that Globe had waived the defense of limitation of consequential damages by not raising it as an affirmative defense in a timely fashion and that, in any event, on the merits Globe would not have prevailed on the defense had it been properly asserted. Judgment was then entered in favor of J & J for the full amount of the verdict.

Globe appealed, challenging only the award of lost profits. We reverse and remand for further proceedings.

Generally, in diversity cases, while state law defines the nature of defenses, the Federal Rules of Civil

Procedure provide the manner and time in which defenses are raised and when waiver occurs. An important factor in deciding if waiver has occurred is whether the plaintiff has suffered prejudice as a result of the delay in presenting the defense. See Healy Tibbetts Construction Co. v. Insurance Co. of North America, 679 F.2d 803, 804 (9th Cir. 1982) (no prejudice to plaintiff found where insurance policy exclusionary clause raised on motion for summary judgment).

After trial in this case, Judge Belloni decided that the defense had been waived because it was presented shortly before trial and the plaintiff would have been unfairly prejudiced by having to change its trial strategy at the last moment. We conclude that the trial judge erred by refusing to allow Globe to present the limitation of

damages defense at trial. See Rivera v. Anaya, 726 F.2d 564, 566 (9th Cir. 1984), citing Healy Tibbetts, 679 F.2d at 804 (liberalization of requirement that affirmative defenses be raised in defendant's initial pleading in the Ninth Circuit); United States for the Use & Benefit of H&S Industries v. Rich, 525 F.2d 760, 767 (7th Cir. 1975). The limitation clause was contained in the written contract upon which plaintiff's complaint was based. Plaintiff was aware of the existence of the clause from the inception of the lawsuit.

The defense to the lost profits claim was first raised by Globe in a pretrial memorandum filed with the court. It was also discussed at the pretrial conference and in a motion after trial for judgment notwithstanding the verdict. The judge ruled before trial that he would allow the plaintiff

to present evidence of lost profits to the jury. Counsel for Globe requested that he be allowed to take a continuing objection to the introduction of such evidence, which request was allowed by the court. Counsel for Globe adequately preserved the issue on the record, even though he failed to make a specific objection to the jury being instructed on how to figure damages for lost profits.

The jury determined that an oral contract existed between Globe and J & J. In his Memorandum and Order denying the defendant's Motion for Judgment Notwithstanding the Verdict, the trial judge rejected Globe's attempt to apply the exculpatory language in the written contract to the oral agreement because they were "two independent contracts involving different parties and supported by separate consideration."

Absent a showing in the oral contract that the parties intended to limit damages the court refused to allow defendant Globe to assert the clause in its defense. This interpretation of the oral contract overlooks the fact that the oral agreement necessarily incorporated the terms of the underlying written contract, for it was completion of the HNA/J & J described in the written agreement that prompted Williams to make his proposals to Bamford in the first place and that without reference to the written contract, the oral contract would be unenforceable as vague and indefinite. Section 8A of the written contract contains the following provision:

> SECTION 8 - GENERAL
>
> A. This agreement contains the entire understanding of the parties and it is intended as a final expression of their agreement and complete

> statement of the terms thereof and shall not be modified except in writing signed by the parties hereto.

The oral agreement was collateral to the terms of the written agreement, but because it was not in writing, could not modify it to exclude the damages limitation clause. Moreover, the evidence concerning the terms of the oral agreement did not indicate that either of the two negotiating parties as much as mentioned the damage limitation clause or in any way inferred that they intended to modify this provision. The clause thus became part of the agreements construed together and, as successor in interest to the seller under the written agreement, defendant Globe should have been allowed to present it as a defense.

The trial court found support for denial of defendant's post-trial motion

in the jury determination that Globe was the alter ego of HNA. As the alter ego of HNA, Globe was a principal and as such was not a surety or guarantor. Citing County Asphalt, Inc. v. Lewis Welding & Engineering Corp., 323 F. Supp. 1300 (S.D. N.Y. 1970), the court stated that because Globe had engaged in "improper conduct" in controlling HNA and causing its breach with J & J, the defendant was estopped from asserting the damages limitation defense. While it is true that bad faith may prevent a defendant from asserting contractual provisions limiting damages, the determination of the existence of bad faith is a question of fact independent of the determination of "improper conduct" in connection with plaintiff's alter ego theory.

On the record as it stands, the enforcement of this collateral oral

contract is not barred by the Statute of Frauds. The trial court addressed the partial performance issue and found that partial performance removed the oral contract from the Statute of Frauds. The evidence supports this finding.

The judgment for plaintiff is reversed and the case is remanded for such further action or proceedings as the trial judge deems necessary for disposition of this case in a manner consistent with this opinion. Appellant shall have its costs on appeal upon filing of a timely bill.

REVERSED AND REMANDED.

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

J & J LOG & LUMBER COMPANY, a New York corporation,	)	No. 84-3788
Plaintiff/Appellee,	)	
v.	)	ORDER*
GLOBE MACHINE MANUFACTURING COMPANY, a Washington corporation,	)	
Defendant/Appellant.	)	

Before: KENNEDY and NORRIS, Circuit Judges, and STEPHENS**, District Judge

The memorandum disposition filed December 2, 1986, is withdrawn. The attached memorandum disposition constitutes the decision of the panel.

*This disposition is not intended for publication ahd shall not be cited as precedent. Ryule 21, Rules of the Ninth Circuit.

**Honorable Albert Lee Stephens, Jr., Senior United States District Judge for the Central District of California, sitting by designation.

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

J & J LOG & LUMBER COMPANY, a New York corporation,	)	No. 84-3788
Plaintiff/Appellee,	)	D.C. No. CV-81-874-BE
v.	)	
GLOBE MACHINE MANUFACTURING COMPANY, a Washington corporation ,	)	MEMORANDUM
Defendant/Appellant.	)	

Appeal from the
United States District Court
for the District of Oregon
Honorable Robert C. Belloni,
District Judge, Presiding
Argued and Submitted:
March 5, 1985 - Portland, Oregon

Before: KENNEDY and NORRIS, Circuit Judges, and STEPHENS**, District Judge

*This disposition is not intended for publication and shall not be cited as precedent. Rule 21, Rules of the Ninth Circuit.

**Honorable Albert Lee Stephens, Jr., Senior United States District Judge for the Central District of California, sitting by designation.

On November 18, 1980, J&J Log entered into a written contract with Hildebrand North America, Inc. (HNA) for the design and construction of six lumber kilns and a wood-fired steam generating system in Dover Plains, New York, J&J's place of business. During negotiations between the parties, J&J insisted on a penalty cause of $500.00 per day in the event that HNA failed to complete the contract by October 31, 1981. HNA, in turn, insisted on limiting its liability for late completion to a maximum late penalty of five percent of the contract price. The contract contained a limited warranty for repair and/or replacement of defective parts. The contract also excluded special or consequential damages sustained by J&J "from any cause."

HNA failed to complete the J&J contract in a timely manner. The contract provided for delivery on or before May 18, 1981. By late summer of 1981, only about 55% of the contract had been performed, although J&J had already paid 80% of the payments it owed under the contract.

HNA never operated on a positive cash flow after 1980. Upon discovering in June 1981 that completion of the J&J/HNA contract would be jeopardized unless HNA received financial assistance, the president of J&J agreed to post a $500,000 letter of credit for HNA's use as operating capital. In return, J&J received an option to purchase five percent of the HNA stock and a security interest in everything owned by HNA and Wood Technology, Inc. (Wood Tech), HNA's parent corporation.

Prior to July 20, 1981, Globe Machine Manufacturing Co., (Globe) owned of the outstanding shares of Wood Tech. In late July, Globe acquired a controlling interest in Wood Tech by obtaining a proxy from another Wood Tech shareholder. Globe then called a meeting of the shareholders of Wood Tech. The president of J&J flew from New York to Oregon to attend the shareholders meeting in order to protect J&J's interest in HNA and Wood Tech. At the meeting, Globe elected new directors and officers for HNA. The new president of Wood Tech and the president of J&J had a private conference that same morning. The parties disagree about exactly what transpired in that conference.

The president of J&J, Williams, testified that the two men agreed that Globe would see that the J&J project was

completed, would post a bond on the project and would release J&J from its underlying letter of credit obligations. In return, Williams claimed, J&J agreed to release its option to purchase 5% of HNA, to pay the balance of the contract price still owing HNA in advance, and to help Globe obtain additional shares in Wood Tech. In contrast, the president of Wood Tech, Bamford, testified that, although he acknowledged Williams' proposals, he was in no position to agree to anything on behalf of Wood Tech at that point, and accordingly, never formed an agreement with Williams.

Work on the J&J contract subsequently ceased, and J&J filed suit against Wood Tech and HNA for the return of its letter of credit. J&J ultimately undertook completion of the project itself, HNA responded by taking certain

actions such as deleting J&J's name from crated equipment sitting in HNA's yard that had been destined for shipment to J&J, and locking up the blueprints and drawings for the J&J job.

J&J completed the project in early June, 1982, at a cost of $262,665.11. The HNA/J&J contract had provided for completion of the kilns by May 17, 1981. J&J filed suit in the district court for breach of contract by Globe. J&J claimed at trial that it had suffered a delay of seven months, a time period figured by a starting date for the penalty clause under the written contract of November 1, 1981, and a completion date for the project of the end of May, 1982.

At trial, J&J proceeded on a breach of contract theory alleging breach of the oral agreement made between the presidents of Wood Tech and J&J at the

Wood Tech's shareholders' meeting, and also claiming that Globe was liable as the alter ego of HNA for breach of the underlying written construction contract. The jury returned a special verdict in favor of plaintiff J&J in which the jury found that an oral contract had been formed between the parties and breached by Globe and, in the alternative, that Globe actually controlled HNA and caused HNA to breach the written agreement. The verdict included an award for the cost of completion of the contract and a separate award for consequential damages in the form of lost profits stemming from the delay in completion of the contract. Judgment was entered in favor of J&J for the full amount of the verdict. Globe appealed, challenging only the award of lost profits. We reverse.

The damage limitation clause as a defense to the lost profits claim was first mentioned by Globe in a pretrial memorandum filed with the court. It was also discussed at the pretrial conference and in a motion after trial for judgment notwithstanding the verdict. The judge ruled before trial that he would allow the plaintiff to present evidence of lost profits to the jury. Counsel for Globe requested that he be allowed to take a continuing objection to the introduction of such evidence, which request was allowed by the court. Counsel for Globe adequately preserved the issue on the record.

After trial in this case, the trial judge decided that the provision in the contract limiting damages had been waived because it was presented shortly before trial and had not been raised as an affirmative defense in the answer or

other pleading and that the plaintiff would have been unfairly prejudiced by having to change its trial strategy at the last moment. We conclude that the trial judge erred in this ruling by refusing to allow Globe to present the limitation of damages clause of the written contract to the jury in opposition to an award of special damages. United States For The Use & Benefit Of H&S Industries v. Rich, 525 F.2d 760, 767 (7th Cir. 1975). The limitation clause was contained in the written contract upon which plaintiff's complaint was based. Plaintiff was aware of the existence of the clause from the inception of the lawsuit. See Healy Tibbetts Construction Co. v. Insurance Co. of North America, 679 F.2d 803, 804 (9th Cir. 1982).

In the judge's post-trial Memorandum and Order Globe's motion for

judgment notwithstanding the verdict was denied. The trial judge ruled that Globe had waived the limitation defense in a timely fashion and that, in any event, Globe's improper conduct estopped it from relying on the clause. These rulings are erroneous as a matter of law.

The limitation of liability clause is not an affirmative defense because it was contained in the written contract upon which plaintiff's complaint was based. Rich, supra. The dispute involving the written contract necessarily involves all the terms of the contract, including the limitation of liability clause. There is no merit to the argument that the terms of a contract that has been introduced into evidence and upon which the action is based must be affirmatively pleaded. By arguing that the clause was an affirma-

tive defense, J&J led the trial judge to commit a reversible error of law that must now be corrected. The clause must be applied to the written contract and to the oral contract as well.

In denying the motion of j.n.o.v., the trial judge also rejected Globe's attempt to apply the exculpatory language in the written contract to the oral agreement because they were "two independent contracts involving different parties and supported by separate consideration." Absent a showing in the oral contract that the parties intended to limit damages, the court refused to allow Globe to assert the clause in its defense. This interpretation of the oral contract overlooks the fact that the oral agreement necessarily incorporated the terms of the underlying written contract. It was completion of the

HNA/J&J project described in the written agreement that prompted Williams to make his proposals to Bamford in the first place. Without reference to the written contract, the oral contract would be unenforceable as vague and indefinite. Section 8A of the written contract contains the following provision:

> This agreement contains the entire understanding of the parties and it is intended as a final expression of their agreement and complete statement of the terms thereof and shall not be modified except in writing signed by the parties hereto.

The oral agreement was collateral to the terms of the written agreement, but because it was not in writing could not modify it to exclude the damage limitation clause. Moreover, the evidence concerning the terms of the oral agreement did not indicate that either of the two negotiating parties as much as mentioned the damage limitation

clause or in any way indicated that they intended to modify this provision. The clause thus became part of the agreements construed together and, as successor in interest to the seller under the written agreement, Globe was entitled to rely and prevail on it.

However, the trial judge held that because Globe had engaged in "improper conduct" in controlling HNA and causing its breach with J&J, Globe was estopped from relying on the damage limitation clause. While bad faith may prevent a defendant from asserting a contractual damage limitation clause, the determination of the existence of bad faith is a question of fact independent of the determination of "improper conduct" in connection with J&J's alter ego theory.

The trial judge's finding that the "improper conduct" constituted bad faith

was clearly erroneous. J&J had the burden of proving bad faith in order to defeat the limitation clause, and it never attempted to establish a bad faith case. J&J's failure to submit a proposed jury instruction on the elements of bad faith is one indication that a bad faith case was not presented. In J&J's proposed jury instruction on the improper conduct issue, J&J cited AMFAC Foods, Inc. International Systems & Controls Corp. 294 Or. 94, 654 P.2d 1092 (1982). C.R. No. 87. This citation merely confirms that J&J never presented a case in bad faith because that case has nothing to do with bad faith defeating a damage limitation clause. In oral argument, J&J attempted to save itself from this failure. It argued that Fed. R. Civ. P. 49(a) permits the trial judge to make a finding on an issue of fact that has

been omitted in the special verdict and that the finding of bad faith was a proper exercise of the trial judge's authority. However, it is an obvious statement of law that a judge may not make a finding of fact on an issue of fact that has not been introduced into the case at trial.

In summary, the following rulings control the disposition of this case. The damage limitation clause did not have to be raised as an affirmative defense. Globe never waived its rights under that clause. The trial judge should have applied the clause to the breach of the written contract. The clause also limits the damages arising out of the breach of the oral contract because the oral contract necessarily incorporated all the terms of the written contract. While a showing of bad faith may defeat the operation of a

damage limitation clause, the clause at sue is effective because J&J never presented a case on the bad faith issue. J&J is entitled to recover for the cost of completion of the contract and nothing more.

The judgment for plaintiff is reversed. Appellant shall have its costs on appeal upon filing of a timely bill.

REVERSED.

I hereby certify that I served the foregoing .....

..... on ..... ,

attorney for ..... on the ..... day of

..... , 19 .. .., by mailing to him three true and correct copies thereof, certified by me as such. I further certify that said copies were placed

in a sealed envelope addressed to the said attorney at .....

.....

which is his regular office address, or his address as last given by him on a document which he has filed in the within entitled cause and served on me; said sealed envelope was then deposited in the United States post office at

..... , Oregon, on the day last above mentioned, with the postage thereon fully paid.

.....

Attorney ..... for

Service of the within .....

is hereby accepted in ..... ,Oregon, this

..... day of ..... , 19 ..... ,

by receiving three copies thereof.

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Attorney ..... for .....